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Section 86-1.20 Less expensive alternatives. Reimbursement for the cost of providing services may be the lesser of the actual costs incurred or those costs which could be reasonably anticipated if such services had been provided by the operation of joint central services or use of facilities or services which could have served as effective alternatives or substitutes for the whole or any part of such service. In this respect, the chief executive officer of a medical facility will be required to submit to the State Department of Health as an attachment to the uniform financial report, effective with report periods beginning on or after January 1, 1977, an affidavit delineating the medical facility's practices of pursuing joint central services or less expensive alternatives. There must be a letter accompanying the affidavit, reflecting the health systems agency's acknowledgment that they have received such affidavit.

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Section 86-1.21 Allowable costs. (a) To be considered as allowable in determining reimbursement rates, costs must be properly chargeable to necessary patient care. Except as otherwise provided in this Part, or in accordance with specific determination by the commissioner, allowable costs shall be determined by the application of the principles of reimbursement developed for determining payments under the title XVIII (Medicare) program.

(b) Allowable costs may not include costs for services that have not been approved by the commissioner.

(c) Allowable cost shall include a monetary value assigned to services provided by religious orders and for services rendered by an owner and operator of a facility.

(d) Allowable costs may not include amounts in excess of reasonable or maximum title XVIII (Medicare) costs or in excess of customary charges to the general public. This provision shall not apply to services furnished by public providers free of charge or at a nominal fee.

(e) Allowable costs shall not include expenses or portions of expenses reported by individual facilities which are determined by the commissioner not to be reasonably related to the efficient production of service because of either the nature or amount of the particular item.

(f) Any general ceilings applied by the commissioner, as to allowable costs in the computation of reimbursement rates, shall be published in a hospital memorandum or other appropriate manner.

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(g) [Reserved]

(h) Allowable costs shall not include costs which principally afford diversion, entertainment or amusement to their owners, operators or employees.

(i) Allowable costs shall not include any interest charged or penalty imposed by governmental agencies or courts, and the costs of policies obtained solely to insure against the imposition of such a penalty.

(j) Allowable costs shall not include the direct or indirect costs of advertising, public relations and promotion except in those instances where the advertising is specifically related to the operation of the facility and not for the purpose of attracting patients.

(k) Allowable costs shall not include costs of contributions or other payments to political parties, candidates or organizations.

(l) Allowable costs shall include only that portion of the dues paid to any professional association which has been demonstrated, to the satisfaction of the commissioner, to be allocable to expenditures other than for public relations, advertising and political contributions. Any such costs shall also be subject to any cost ceilings that may be promulgated by the commissioner pursuant to subdivision (f) of this section.

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(m) [Reserved]

(n) Allowable costs shall not include any element of cost, as determined by the commissioner, to have been created by the sale of a medical facility.

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Section 86-1.22 Recoveries of expense. Operating costs shall be reduced by the cost of services and activities which are not properly chargeable to patient care. In the event that the State Commissioner of Health determines that it is not practical to establish the costs of such services and activities, the income derived therefrom may be substituted for costs of these services and activities. Examples of activities and services covered by this provision include:

- (a) drugs and supplies sold for use outside the medical facility;
- (b) telephone and telegraph services for which a charge is made;
- (c) discount on purchases;
- (d) living quarters rented to employees;
- (e) employee cafeterias;
- (f) meals provided to special nurses or patients' guests;
- (g) operation of parking facilities for community convenience;
- (h) lease of office and other space of concessionaries providing services not related to medical service;
- (i) tuitions and other payments for educational service, room and board and other services not directly related to medical service.

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86-1.23 Depreciation. (a) Reported depreciation based on historical cost is recognized as a proper element of cost. Useful lives shall be the higher of the reported useful life or those useful lives from the Estimated Useful Lives of Depreciable Hospital Assets, 1983 edition, American Hospital Association, consistent with title XVIII provisions. This regulation is effective for depreciable assets purchased on or after January 1, 1978. Copies of this publication are available from the American Hospital Association, 840 North Lake Shore Drive, Chicago, IL 60611, and a copy is available for inspection and copying at the offices of the records access officer of the Department of Health, Corning Tower, Empire State Plaza, Albany, NY 12237.

(b) In the computation of rates effective January 1, 1975 for voluntary facilities, depreciation shall be included on a straight-line method on plant and nonmovable equipment. Depreciation on movable equipment may be computed on a straight line method or accelerated under a double declining balance or sum-of-the-years' digit method. Depreciation shall be funded unless the Commissioner of Health shall have determined, upon application by the facility, and after inviting written comments from interested parties, that the requested waiver of the requirements for funding is a matter of public interest and necessity. Effective with the fiscal year starting on or after January 1, 1981 in instances where funding is required (that being the transfer of monies to the funded accounts), depreciation on major movable equipment shall be funded in the year revenue is received from the reimbursement of each expense and in the amount included in reimbursement for that year. In instances where funding is required, such fund may be used only for capital expenditures with approval as required for the amortization of capital indebtedness. Funding for plant and fixed equipment shall mean that the transfer of monies to the funded accounts shall occur by the end of the fiscal period in which the depreciation is recorded. Board-designated funds and the accrual of liabilities to the funded depreciation accounts (due to/from accounts) shall not be recognized as funding of depreciation. Deposits to the funded depreciation accounts must remain in such accounts [for six months or more] to be considered as valid funding transactions unless expended for the purposes for which it was funded.

(c) In the computation of rates effective January 1, 1975 for public facilities, depreciation is to be included on a straight-line method on plant and nonmovable equipment. Depreciation on movable equipment may be computed on a straight-line method or accelerated under a double declining balance or sum-of-the-years' digits method.

(d) In the computation of reimbursement rates for proprietary facilities, depreciation is to be computed on a straight-line basis on plant and nonmovable equipment. Depreciation on movable equipment may be computed on a straight-line method or accelerated under a double declining balance or sum-of-the-years' digits method.

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(e) Medical facilities financed by mortgage loans pursuant to the Nursing Home Companies Law or the Hospital Mortgage Loan Construction Law shall conform to the requirements of this Subpart. In lieu of depreciation and interest, on the loan financed portion of the facilities, the State Commissioner of Health shall allow level debt service on the mortgage loan, for all loans approved for financing prior to January 1, 1990, together with such required fixed charges, sinking funds and reserves as may be determined by the Commissioner as necessary to assure repayment of mortgage indebtedness. For loans approved for financing on or after January 1, 1990, medical facilities shall receive reimbursement in the form of interest and depreciation in accordance with the remainder of this Subpart.

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Section 86-1.24 Interest. (a) Necessary interest on both current and capital indebtedness is an allowable cost for all medical facilities.

(b) To be considered as an allowable cost, interest shall be incurred to satisfy a financial need, and at a rate not in excess of what a prudent borrower would have had to pay in the money market at the time the loan was made. Also, the interest shall be paid to a lender not related through control, ownership, affiliation or personal relationship to the borrower, except in instances where the prior approval of the Commissioner of Health has been obtained. Financial need for capital indebtedness relating to a specified project shall exist when all available restricted funds designated for capital acquisition of that type have been considered for equity purposes.

(c) Interest expense shall be reduced by investment income with the exception of income from funded depreciation, qualified pension funds, trusteed malpractice insurance funds, or in instances where income from gifts or grants is restricted by donors. Interest on funds borrowed from a donor restricted fund or funded depreciation is an allowable expense. Investment income shall be defined as the aggregate net amount realized from dividends, interest, rental income, interest earned on temporary investment of withholding taxes, as well as all gains and losses. If the aggregate net amount realized is a loss, the loss shall not be allowable. Rate year investment income shall reduce rate year interest expense allowed for reimbursement as follows:

(i) for all medical facilities, investment income shall

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(ii) any remaining amount of investment income, after application of paragraph (i), shall be used to reduce capital interest expense reimbursed that year for medical facilities; and

(iii) any remaining amount of investment income after application of paragraph (ii) shall not be considered in the determination of allowable costs.

(d) Interest on current indebtedness shall be treated and reported as an operating, administrative expense.

(e) Interest on capital indebtedness is an allowable cost if the debt generating the interest is approved by the commissioner, incurred for authorized purposes, and the principal of the debt does not exceed either the approval of the commissioner or the cost of the authorized purposes.

Capital indebtedness shall mean all debt obligations of a facility that are:

(1) evidenced by a mortgage note or bond and secured by a mortgage on the land, building or nonmovable equipment; a note payable secured by the nonmovable equipment of a facility; a capital lease;

(2) incurred for the purpose of financing the acquisition, construction or renovation of land, building or nonmovable equipment;

(3) found by the commissioner to be reasonable, necessary and in the public interest with respect to the facility. Interest related to refinancing indebtedness shall be considered an allowable cost only to

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the extent that it is payable with respect to an amount equal to the unpaid principal of the indebtedness then being refinanced. However, interest incurred on refinanced debt in excess of the previously unpaid balance of the refinanced indebtedness will be allowable on acceptance demonstration to the Commissioner of Health that such refinancing will result in a debt service savings over the life of the indebtedness; or

(4) incurred for the purpose of advance refunding of debt. [Losses] Gains and losses resulting from the advanced refunding of debt shall be treated and reported as a deferred charge or asset. This deferred charge or asset is to be amortized on a straight-line basis ~~over the period to the~~ scheduled maturity date of the refunding debt.

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(f) Where a public finance authority has established a mortgage rate of interest such that sufficient cash flows exist to retire the mortgage prior to the stated maturity, the amount of the mortgage to be forgiven, at the time of such forgiveness, shall be capitalized as a deferred asset and amortized over the remaining mortgage life, as a reduction to the facility's capital expense.

(g) Voluntary facilities shall report mortgage obligations, financed by public finance authorities for their benefit and which they are responsible to repay, as liabilities in the general fund, when such mortgage obligations are incurred.

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